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What Is In A Non Disclosure Confidentiality Agreement

The prospective acquirer is often asked to execute a confidentiality and/or nondisclosure agreement usually provided by the intermediary for the seller. The seller does not want to reveal financial and other confidential information regarding the business to a potential acquirer without the protection of a nondisclosure agreement. This agreement has a three-fold purpose. It will provide:

1. That the acquirer is to hold confidential all information provided to the acquirer about the business,
2. For the acquirer to not use any such information other than for evaluation of the proposed purchase of the business, and
3. For the acquirer to return all information to the seller if the sale does not close.

Protected Information The definition of what is considered protected information is something that should be considered by each party. The seller may want a more expansive definition of what is considered to be protected information. The acquirer, on the other hand, will desire a more narrow definition. Oftentimes the acquirer and seller will agree to create exceptions for information previously known to the acquirer as well as common industry and public knowledge. Information already in the public domain will always be excluded.

Prior Knowledge If the acquirer is already involved with the company and has company knowledge, e.g. a current employee, supplier, or customer - then the term "information" has a different definition. The agreement should exclude the knowledge that has already been obtained by the acquirer as a result of his or her connection with the company. Otherwise, the omission could lead to the employee, supplier or customer signing the equivalent of a non-competition agreement or the supplier not being allowed to operate a related business.

If a prospective acquirer desires to purchase a business within a certain industry and already has information that could be considered confidential to the seller, there needs to be a special carve-out within the nondisclosure agreement. This action works to prevent the seller from enjoining the acquirer from acquiring a competitor of the seller. Likewise, information already in the public domain will always be excluded from such agreements.

Persons Covered Those covered under the agreement carry separate intentions between seller and acquirer. A seller may want a specific list of people to whom the information can be released; whereas, the acquirer may want it to apply generally to all of the acquirer's employees, with a need to know, and agents such as a law firm or an

outside CPA firm. The latter provision is preferable so there is no inadvertent disclosure to an agent who was not specifically named in the nondisclosure agreement.

The receiving party of any confidential information, usually the acquirer, will be responsible for any improper dissemination of the information to a third-party by its agents. However, an acquirer will generally want to add language to provide protection to the acquirer to provide that the acquirer is:

- Not liable if the acquirer or its representatives used the same degree of care in protecting the information as the seller uses in protecting the information, and
- Not liable if the acquirer uses the same degree of care in protecting its own proprietary information.

Third-Party Disclosures Another issue is the level of protection the acquirer needs to provide if the information is sought by a third-party. It is common practice for the acquirer to have to notify the seller of any attempt by a third party to seek confidential information disclosure pursuant to law.

The question arises whether the acquirer is required to use its best efforts to obtain reliable assurances that the information will continue to be treated confidentially. For example, an acquirer will not want to pay attorneys fees to defend the confidentiality of the seller's information.

To address this situation, the confidentiality agreement can provide for the acquirer to make "reasonable" efforts to obtain an assurance the information will be treated as confidential by the third-party, or the seller will provide for the costs of negotiating the disclosure and providing payment for the acquirer's legal fees.

Non-Disclosure Timeframe Generally, the nondisclosure agreement will provide for the return of all protected information if:

- A letter of intent is not signed by a certain date, or
- If a party decides that it does not wish to proceed with the proposed acquisition, or
- If the acquisition is not consummated.

There should also be some definable time in the future when the protected information will no longer be treated as confidential; after that date the agreement will not be enforceable. This date is typically two to five years in the future.

Enforcement With respect to enforcement, language may be included in the agreement that provides for injunctive relief without proof of damages. This clause would often provide for the recovery of attorney's fees by the prevailing party and that no bond is required. If the acquirer is an entity, the individual owners may be asked to personally sign a confidentiality agreement to assure personal compliance as well as corporate compliance.

Staged Information Release. A Seller should stage when and how confidential information is actually disclosed and released. Because company information is critical

to operations, an outside person's ability to use such information to the detriment of the seller, even with a signed confidentiality agreement, should be considered. The seller will be very careful with respect to what information is provided to the prospective acquirer at what time throughout the process. The disclosure of information may often be given in different stages during the acquisition process with the more sensitive information being provided later in the process. For example, the acquirer will often receive customer lists and key vendor and supplier lists shortly before the closing date.

Direct Competitors The issue of non-disclosure and confidentiality is not normally a difficult one to get beyond except in the case of direct competitors. Then the concerns about customer information, proprietary technology, unique processes, financials, market strategy and employees can become real troublesome on both sides. The seller does not want his competitor to know about his business, and the competitor does not want such information either. The acquirer does not want to have the technology that is in the works, employee hires or processes they plan to implement be subject to an unrelated lawsuit in the event the transaction is not consummated.

Conclusion. In conclusion, the non-disclosure confidentiality agreement is the first step in the acquisition process and is typically present in every acquisition transaction discussions. The language used is consistently applied and as such is normally not a source of impediment in the acquisition process.